

FIRST STEP HOUSE, INC.

FINANCIAL STATEMENTS

JUNE 30, 2006 and 2005

FIRST STEP HOUSE, INC.

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► Lake, Hill & Myers

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CERTIFIED PUBLIC ACCOUNTANTS

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INDEPENDENT AUDITORS' REPORT

October 30, 2006

To the Board of Directors and Management of
First Step House, Inc.

We have audited the accompanying statement of financial position of First Step House, Inc. (a nonprofit organization) as of June 30, 2006 and 2005 and the related statements of activities and change in net assets, functional expenses and cash flows for the years then ended. These financial statements are the responsibility of the Organization's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of First Step House, Inc. as of June 30, 2006 and 2005, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 30, 2006 on our consideration of First Step House Inc.'s internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Our audits were performed for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

Lake, Hill & Myers

FIRST STEP HOUSE, INC.
STATEMENT OF FINANCIAL POSITION

<u>ASSETS</u>	<u>June 30,</u>	
	<u>2006</u>	<u>2005</u>
Current assets:		
Cash	\$ 288,168	\$ 9,868
Grants and contracts receivable	275,747	188,387
Other receivables	7,611	27,559
Prepaid expenses	3,676	3,892
Deposits	<u>1,088</u>	<u>-</u>
Total current assets	<u>576,290</u>	<u>229,706</u>
Property and equipment, net	<u>801,902</u>	<u>821,372</u>
	<u>\$1,378,192</u>	<u>\$1,051,078</u>
 <u>LIABILITIES AND NET ASSETS</u>		
Current liabilities:		
Accounts payable	\$ 36,535	\$ 35,921
Accrued expenses	91,664	73,140
Line of credit payable	-	12,937
Current portion of long-term debt	<u>18,589</u>	<u>17,648</u>
Total current liabilities	<u>146,788</u>	<u>139,646</u>
Long-term liabilities:		
Long-term debt, less current portion	<u>560,696</u>	<u>578,980</u>
Total long-term liabilities	<u>560,696</u>	<u>578,980</u>
Net assets:		
Unrestricted	<u>670,708</u>	<u>332,452</u>
	<u>\$1,378,192</u>	<u>\$1,051,078</u>

See notes to financial statements.

FIRST STEP HOUSE, INC.

STATEMENT OF ACTIVITIES AND CHANGE IN NET ASSETS

	<u>Year ended June 30,</u>	
	<u>2006</u>	<u>2005</u>
Unrestricted net assets:		
Public support and revenue:		
Salt Lake County - State and County	\$ 898,027	\$ 417,303
Salt Lake County - Federal	363,070	217,715
Veterans Administration	506,907	372,943
Volunteers of America	56,000	56,000
Food stamps	41,790	50,744
Utah County substance abuse	41,094	34,376
Utah Department of Health	15,146	-
Mental Health Court/Housing Authority of SL County	54,000	27,946
Public support	16,638	33,607
Program income - client fees	271,398	334,900
Interest income	1,841	32
Other income	<u>7,009</u>	<u>10,917</u>
Total unrestricted public support and revenue	<u>2,272,920</u>	<u>1,556,483</u>
Expenses:		
Alcohol and drug rehabilitation	<u>1,683,373</u>	<u>1,252,288</u>
Total program services	<u>1,683,373</u>	<u>1,252,288</u>
Management and general	148,453	125,400
Fundraising	<u>102,838</u>	<u>85,401</u>
Total supporting services	<u>251,291</u>	<u>210,801</u>
Total expenses	<u>1,934,664</u>	<u>1,463,089</u>
Increase in unrestricted net assets	338,256	93,394
Unrestricted net assets at beginning of year	<u>332,452</u>	<u>239,058</u>
Unrestricted net assets at end of year	<u>\$ 670,708</u>	<u>\$ 332,452</u>

See notes to financial statements.

FIRST STEP HOUSE, INC.
STATEMENT OF FUNCTIONAL EXPENSES
FOR THE YEAR ENDED JUNE 30, 2006

	Program services expenses	Supporting services expenses			
	Alcohol and drug rehabilitation	Management and general	Fundraising	Total	Total expenses
Personnel	\$ 997,048	\$ 118,191	\$ 96,976	\$ 215,167	\$ 1,212,215
Contract services	53,171	5,259	-	5,259	58,430
Contract services - Project Reality	192,771	-	-	-	192,771
Food	72,965	-	-	-	72,965
House and kitchen supplies	60,380	-	-	-	60,380
House repairs and maintenance	29,043	2,872	-	2,872	31,915
Utilities	55,346	5,474	-	5,474	60,820
Insurance	26,446	2,615	-	2,615	29,061
Office supplies	13,657	1,619	1,328	2,947	16,604
Interest	24,499	2,904	2,383	5,287	29,786
Travel and training	25,799	2,552	-	2,552	28,351
Miscellaneous	14,028	1,663	1,364	3,027	17,055
Telephone	8,087	959	787	1,746	9,833
Rent	22,964	-	-	-	22,964
Recreation for residents	43,240	-	-	-	43,240
Depreciation	43,929	4,345	-	4,345	48,274
Total Expenses	<u>\$ 1,683,373</u>	<u>\$ 148,453</u>	<u>\$ 102,838</u>	<u>\$ 251,291</u>	<u>\$ 1,934,664</u>

See notes to financial statements.

FIRST STEP HOUSE, INC.
STATEMENT OF FUNCTIONAL EXPENSES
FOR THE YEAR ENDED JUNE 30, 2005

	Program services expenses	Supporting services expenses			
	Alcohol and drug rehabilitation	Management and general	Fundraising	Total	Total expenses
Personnel	\$ 803,968	\$ 95,303	\$ 78,197	\$ 173,500	\$ 977,468
Contract services	62,184	6,150	-	6,150	68,334
Food	76,114	-	-	-	76,114
House and kitchen supplies	62,155	-	-	-	62,155
House repairs and maintenance	28,055	2,775	-	2,775	30,830
Utilities	41,349	4,089	-	4,089	45,438
Insurance	22,203	2,196	-	2,196	24,399
Office supplies	20,776	2,463	2,021	4,484	25,260
Interest	30,371	3,600	2,954	6,554	36,925
Travel and training	14,639	1,448	-	1,448	16,087
Miscellaneous	717	1,428	1,172	2,600	3,317
Telephone	10,869	1,288	1,057	2,345	13,214
Rent	21,600	-	-	-	21,600
Recreation for residents	10,174	-	-	-	10,174
Depreciation	47,114	4,660	-	4,660	51,774
Total Expenses	<u>\$ 1,252,288</u>	<u>\$ 125,400</u>	<u>\$ 85,401</u>	<u>\$ 210,801</u>	<u>\$ 1,463,089</u>

See notes to financial statements.

FIRST STEP HOUSE, INC.
STATEMENT OF CASH FLOWS

	<u>Year ended June 30,</u>	
	<u>2006</u>	<u>2005</u>
Cash flows from operating activities:		
Cash received from contributions, government, contracts and clients	\$ 2,182,319	\$ 1,478,008
Interest received	1,841	32
Cash paid to vendors and employees	(1,818,390)	(1,330,138)
Interest paid	<u>(29,786)</u>	<u>(35,321)</u>
Net cash provided by operating activities	<u>335,984</u>	<u>112,581</u>
Cash flows from investing activities:		
Increase in property and equipment	(28,804)	(5,000)
Proceeds from the sale of property and equipment	<u>1,400</u>	<u>-</u>
Net cash used in investing activities	<u>(27,404)</u>	<u>(5,000)</u>
Cash flows from financing activities:		
Decrease in line of credit	(12,937)	(84,058)
Principal payments on long-term debt	<u>(17,343)</u>	<u>(14,981)</u>
Net cash used in financing activities	<u>(30,280)</u>	<u>(99,039)</u>
Net increase in cash	278,300	8,542
Cash at beginning of year	<u>9,868</u>	<u>1,326</u>
Cash at end of year	<u>\$ 288,168</u>	<u>\$ 9,868</u>

(continued)

See notes to financial statements.

FIRST STEP HOUSE, INC.
STATEMENT OF CASH FLOWS

(continued)

	<u>Year ended June 30,</u>	
	<u>2006</u>	<u>2005</u>
Reconciliation of change in net assets to net cash provided by operating activities:		
Change in net assets	\$338,256	\$ 93,394
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation	48,274	51,774
Gain on the sale of property and equipment	(1,400)	-
Change in assets and liabilities:		
Increase in grants receivable	(87,360)	(78,443)
Decrease (increase) in other receivables	19,948	(23,460)
Decrease in prepaid expenses	216	196
Increase in deposits	(1,088)	-
Increase in accounts payable	614	16,209
Increase in accrued expenses	<u>18,524</u>	<u>52,911</u>
Net cash provided by operating activities	<u>\$335,984</u>	<u>\$ 112,581</u>

Schedule of non-cash investing and financing activities:

None.

See notes to financial statements.

FIRST STEP HOUSE, INC.
NOTES TO FINANCIAL STATEMENTS

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

Operational Purpose

First Step House, Inc. (First Step) is a nonprofit corporation organized under the laws of the State of Utah on December 14, 1958. The Organization is a residential alcoholism treatment center providing alcohol and drug rehabilitation services. The Organization maintains additional facilities (apartment complexes) for graduates of the treatment program in order to provide them with a sober living environment, and also provides outpatient services. The Organization receives its funding from government grants, client fees, food stamps, and private/individual donations.

First Step's principal program is as follows:

Alcohol and drug rehabilitation - to help low/no income, often-homeless individuals, achieve long-term recovery from the dysfunctional effects of substance abuse and to return to society as meaningfully employed and responsible individuals.

Financial Statement Presentation

The accompanying financial statements of First Step have been prepared using the accrual method of accounting and accordingly reflect all significant receivables, payables and other liabilities.

First Step reports information regarding its financial position and activities according to the following three classes of net assets:

Unrestricted - accounts for unrestricted assets (net of related liabilities) available for support of the Organization's operations. Assets designated by the Board of Directors for a specific purpose also are accounted for in this fund.

Temporarily Restricted - accounts for resources currently available for use, but expendable only for purposes specified by the donor.

Permanently Restricted - accounts for gifts requiring in perpetuity that the principal be invested and the income only be used.

Property and Equipment

Property and equipment are recorded at acquisition cost or, where donated, at estimated market value at the date of the donation. Depreciation is computed using the straight-line method based on estimated useful lives ranging from 5 to 40 years. Expenditures for repairs and maintenance are charged to expense as incurred.

Cash Equivalents

For purposes of reporting cash flows, cash and cash equivalents are defined as cash on hand and highly liquid investments with original maturities of three months or less.

Allowance for Doubtful Accounts

No allowance for doubtful accounts is provided as management believes all receivables are fully collectible.

Donated Services

Amounts for donated services are reflected in the financial statements if the services create or enhance nonfinancial assets or if First Step would be required to pay for the services if not donated. No amounts have been reflected in the financial statements for donated services. However, many individuals volunteer their time and perform a variety of tasks that assist First Step in completing the goals of its program.

Contributions

Contributions are recorded as revenue when cash is received or First Step receives an unconditional promise to give from the donor. All contributions are available for unrestricted use unless specifically restricted by the donor.

Support that is restricted by the donor is reported as an increase in unrestricted net assets if the restriction expires in the reporting period in which the support is recognized. All other donor-restricted support is reported as an increase in temporarily or permanently restricted net assets, depending on the nature of the restriction. When a restriction expires (that is, when a stipulated time restriction ends or purpose restriction is accomplished), temporarily restricted net assets are reclassified to unrestricted net assets and reported in the Statement of Activities as net assets released from restrictions.

Government Funding

Funding from all government sources is considered to be unrestricted as long as the amounts are expended under contract guidelines and is expended in the period for which it is contracted.

Nonprofit Status

First Step was organized as a nonprofit corporation in accordance with the laws of the State of Utah and is exempt from federal income taxation under provisions of Section 501(c)(3) of the Internal Revenue Code.

Functional Expenses

First Step allocates its expenses on a functional basis among its program and supporting services. Expenses that can be identified with First Step's program or supporting services are directly classified to program or services. Other expenses that are common to several functions are allocated on a reasonable and systematic basis.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

NOTE 2 - GRANTS AND CONTRACTS RECEIVABLE:

Grants and contracts receivable consist of the following:

	<u>June 30,</u>	
	<u>2006</u>	<u>2005</u>
Salt Lake County	\$203,072	\$117,718
Veterans Administration	69,051	60,980
Utah County	3,624	5,022
Volunteers of America	-	4,667
	<u>\$275,747</u>	<u>\$188,387</u>

NOTE 3 - PROPERTY AND EQUIPMENT:

Property and equipment consists of the following:

	<u>June 30,</u>	
	<u>2006</u>	<u>2005</u>
Land	\$ 163,894	\$ 163,894
Buildings and improvements	1,051,573	1,050,562
Furniture and equipment	210,095	182,302
Vehicles	31,503	44,098
	1,457,065	1,440,856
Less accumulated depreciation	<u>(655,163)</u>	<u>(619,484)</u>
	<u>\$ 801,902</u>	<u>\$ 821,372</u>

NOTE 4 - LEASE COMMITMENTS:

First Step currently leases a house from a related party (see Note 9) under a long-term lease agreement that expires in December, 2007. The house is used to house graduates of the program as a transitional housing unit. The monthly rental amount under this agreement is \$1,800. During the years ended June 30, 2006 and 2005, lease expense totaled \$21,600. Future minimum payments due under this lease agreement are as follows:

<u>Year ending June 30,</u>	
2007	\$21,600
2008	10,800
	<u>\$32,400</u>

NOTE 5 - RETIREMENT PLAN:

First Step has established a defined contribution retirement plan (the Plan) for the benefit of its employees. Contributions to the Plan are determined by the Board of Directors. An employee must meet certain eligibility requirements in order to participate in the Plan. During the years ended June 30, 2006 and 2005, First Step did not make any matching contributions to the Plan.

NOTE 6 - CONCENTRATIONS:

First Step's cash is held in federally insured bank accounts. The cash balance exceeds the federally insured limit by approximately \$188,000. Management does not believe this represents a material credit risk.

The majority of First Step's contract revenues are provided through Salt Lake County and the Veterans Administration. A loss of this support would have a materially adverse effect on First Step.

NOTE 7 - LINE OF CREDIT:

First Step maintains an unsecured line of credit agreement with a bank in the amount of \$150,000. The line of credit accrues interest at an interest rate of 1.5 percent plus the bank's "base" rate (9.75 percent at June 30, 2006). At June 30, 2005, the amount owed on the line of credit was \$12,937. During the year ended June 30, 2006, the line of credit was repaid and the balance at June 30, 2006, is \$0.

NOTE 8 - LONG-TERM DEBT:

Long-term debt consists of the following:

	<u>June 30,</u>	
	<u>2006</u>	<u>2005</u>
Mortgage note payable, monthly principal and interest payments of \$1,810, interest at 6.75 percent, due June 15, 2013, secured by property.	\$217,222	\$ 223,830
Note payable, monthly principal and interest payments of \$453, interest at 5.00 percent, due September 1, 2016, secured by equipment.	42,111	45,430
Mortgage note payable, monthly principal payments of \$200, non-interest bearing, due October 1, 2027, secured by property.	149,870	152,270
Mortgage note payable, monthly principal and interest payments of \$563, interest at 6.50 percent, due November 10, 2013, secured by property.	70,089	72,156

Mortgage note payable, monthly principal and interest payments of \$804, interest at 6.50 percent, due November 10, 2013, secured by property.

	<u>99,993</u>	<u>102,942</u>
	579,285	596,628
Less current portion	<u>(18,589)</u>	<u>(17,648)</u>
	<u>\$560,696</u>	<u>\$ 578,980</u>

Future maturities of mortgages payable are as follows:

Year ending June 30,

2007	\$ 18,589
2008	19,568
2009	20,745
2010	21,933
2011	23,199
Thereafter	<u>475,251</u>
	<u>\$579,285</u>

NOTE 9 - RELATED PARTY TRANSACTIONS:

First Step leases a house from an employee under a long-term lease agreement that expires in December, 2007. The monthly rental amount under this agreement is \$1,800. During the years ended June 30, 2006 and 2005, rent expense under this lease agreement was \$21,600.

ADDITIONAL INFORMATION

FIRST STEP HOUSE, INC.
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
YEAR ENDED JUNE 30, 2006

<u>Federal Grantor/Pass-Through Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Pass-through Number</u>	<u>Grant Expenditures</u>
<u>United States Department of Health and Human Services</u>			
Pass-through from Salt Lake County	93.959	AL-05516C	\$363,070
<u>United States Department of Veteran Affairs</u>			
Veterans Administration*	64.024	V660P-4812	136,894
Veterans Administration*	64.024	per diem	164,105
Veterans Administration*	64.024	04-303-UT	205,908
<u>United States Department of Housing & Urban Development</u>			
Volunteers of America	14.235	-	<u>56,000</u>
			<u>\$925,977</u>

* - denotes major program

NOTE A - GENERAL:

The schedule of expenditures of federal awards presents the activity of all federal award programs of First Step House, Inc. (First Step). The First Step reporting entity is defined in Note 1 to First Step's financial statements. All federal financial awards received directly from federal agencies as well as federal financial awards passed through from other government agencies are included on the schedule.

NOTE B - BASIS OF ACCOUNTING:

The accompanying schedule of expenditures of federal awards is presented on an accrual basis of accounting. Grant expenditures are recognized as funds are spent or accrued. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, "Audits of States, Local Governments, and Non-Profit Organizations." Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of the basic financial statements.

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REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

October 30, 2006

To the Board of Directors and Management of
First Step House, Inc.

We have audited the financial statements of First Step House, Inc. as of and for the year ended June 30, 2006, and have issued our report thereon dated October 30, 2006. We have conducted our audit in accordance with auditing standards generally accepted in the United States of America, and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered First Step House, Inc.'s internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be a material weakness. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses. However, we noted other matters involving the internal control over financial reporting, which we have reported to management of First Step House, Inc. in a separate letter dated October 30, 2006.

Compliance

As part of obtaining reasonable assurance about whether First Step House, Inc.'s financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the audit committee, management, board of directors, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

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REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

October 30, 2006

To the Board of Directors and Management of
First Step House, Inc.

Compliance

We have audited the compliance of First Step House, Inc. (a nonprofit organization) with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2006. First Step House, Inc.'s major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of First Step House, Inc.'s management. Our responsibility is to express an opinion on First Step House, Inc.'s compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about First Step House, Inc.'s compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of First Step House, Inc.'s compliance with those requirements.

In our opinion, First Step House, Inc. complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2006.

Internal Control Over Compliance

The management of First Step House, Inc. is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered First Step House, Inc.'s internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts, and grants caused by error or fraud that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of the audit committee, board of directors, management and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Lake, Hill & Myers

FIRST STEP HOUSE, INC.
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2006

Summary of Auditors' Results

- i. The auditor issued an unqualified opinion on the financial statements of the Organization.
- ii. There are no reportable conditions or material weaknesses in internal control over the financial statements disclosed as a result of the audit of the financial statements.
- iii. The auditor noted no noncompliance which is material to the financial statements of the Organization.
- iv. There are no reportable conditions or material weaknesses in internal control over major programs disclosed as a result of the audit of the financial statements.
- v. The auditor issued an unqualified opinion on compliance with requirements applicable to each major program.
- vi. The auditor identified no findings reported under the caption of Audit Findings.
- vii. Major program consists of:

Federal Grantor/Pass-Through Grantor/Program Title	Federal CFDA Number	Expenditures
United States Department of Veteran Affairs: Veterans Administration Alcohol and Drug Rehabilitation	64.024	\$ 506,907

- viii. The Organization had two Type A programs for the year ended June 30, 2006. The dollar threshold to distinguish Type A and Type B programs was \$300,000. Programs were selected to meet the percentage coverage rule of OMB Circular A-133 paragraph _____.520(f).
- ix. The Organization qualifies as a low risk auditee under paragraph .530 of OMB Circular A-133.

Audit Findings

There are no audit findings resulting from the audit.

FIRST STEP HOUSE, INC.
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2005

Ref

Finding

There are no prior audit findings.

► Lake, Hill & Myers

A PROFESSIONAL CORPORATION
CERTIFIED PUBLIC ACCOUNTANTS

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INDEPENDENT ACCOUNTANT'S REPORT ON STATE LEGAL COMPLIANCE

October 30, 2006

To the Board of Directors and Management of
First Step House, Inc.

We have audited the financial statements of First Step House, Inc., a nonprofit corporation, for the year ended June 30, 2006, and have issued our report thereon dated October 30, 2006. As part of our audit, we have audited First Step House Inc.'s compliance with the requirements of the provider contract determined to be a major State assistance program as required by the State of Utah Legal Compliance Audit Guide for the year ended June 30, 2006. First Step House, Inc. received the following major State assistance program from the State of Utah:

Alcohol and Drug Abuse Treatment

(Utah Department of Human Services) – Passed through from Salt Lake County

The management of First Step House, Inc. is responsible for its compliance with all compliance requirements of the contract identified above. Our responsibility is to express an opinion on compliance with those requirements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether material noncompliance with the requirements of the contract referred to above occurred. An audit includes examining, on a test basis, evidence about First Step House, Inc.'s compliance with those requirements. We believe that our audit provides a reasonable basis for our opinion.

The results of our audit procedures disclosed immaterial instances of noncompliance with the requirements referred to above, which are described in the accompanying management letter. We considered these instances of noncompliance in forming our opinion on compliance, which is expressed in the following paragraph.

In our opinion, First Step House, Inc. complied, in all material respects, with the requirements governing types of services allowed or unallowed; matching, level of effort, or earmarking; and special tests and provisions that are applicable to its major State assistance program for the year ended June 30, 2006.

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October 30, 2006

To the Board of Directors and Management
of First Step House, Inc.

In planning and performing our audit of the financial statements of First Step House, Inc. for the year ended June 30, 2006, we considered the Organization's internal control in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on internal control.

However, during our audit, we became aware of various matters that are opportunities for strengthening internal controls and operating efficiency. This letter does not affect our report, dated October 30, 2006, on the financial statements of First Step House, Inc.

We will review the status of these comments during our next audit engagement. We have already discussed these comments and suggestions with various Organization personnel, and we will be pleased to discuss these comments in further detail at your convenience, to perform any additional study of these matters, or to assist you in implementing the recommendations. Our comments are summarized as follows:

Client Receivables

We noted that receivables from clients are not tracked or recorded by the Organization. Currently, the Organization records client co-pay and client self-pay amounts as revenue when payment is received rather than recording client receivables at the time services are rendered. We recommend that the Organization implement policies and procedures to track and record client receivables, particularly at year end.

Management's Response

We concur with the recommendation and will implement policies and procedures to track and record client receivables.

In-Kind Contributions

We noted that the Organization receives numerous donations for essential items pertinent to the success of its program, and that the donations and the use of those donations are not recorded in its financial statements. It is important for the Organization to record the actual cost of providing services to its clients, even if the Organization did not directly pay for the items. This is most

notable in food donations received by the Organization that the Organization would pay for had the food not been donated. We recommend that the Organization develop a policy to record these types of in-kind contributions.

Management's Response

We concur with the recommendation and will develop a policy and procedures to better track in-kind contributions.

Incomplete Personnel Files

We noted that one of ten personnel files selected for testing did not contain a form I-9. For another personnel file selected for testing, we noted a discrepancy between the number of exemptions on form W-4 and the actual number of exemptions used calculate this employee's net payroll. We recommend that policies and procedures be implemented to ensure personnel files are complete and that data used to calculate payroll is accurate.

Management's Response

We concur with the recommendation and will ensure that personnel files are complete and that employee data used to calculate payroll is accurate.

Pre-Audit Conference

We noted that the Organization did not invite its contract provider to its pre-audit conference. We recommend that the Organization invite its contract provider to both the pre- and post-audit conferences.

Management's Response

We concur with the recommendation and will invite our contract provider to future pre-audit conferences. We will also invite our contract provider to the post-audit conference for the current year audit as well as future audits.

We wish to thank Shawn McMillen, Executive Director, and his staff for their support and assistance during our audit.

These comments and recommendations are intended solely for the information and use of the Board of Directors, management, and others within the Organization and should not be used by anyone other than these specified parties.

Lake, Hill & Myers